

Movants' HTA Exhibit 124

National Council on Governmental Accounting Statement 1 Governmental Accounting and Financial Reporting Principles

STATUS

Issued: March 1979

Effective Date: Fiscal years ending after June 30, 1980

Affects: Restates 1968 GAAFR, incorporating "pertinent aspects of 'Audits of State and Local Governmental Units' (ASLGU), the 1974 industry audit guide of the American Institute of Certified Public Accountants (AICPA), as amended" (As of the issuance date of NCGAS 1, the ASLGU had been amended by AICPA SOPs 75-3, 77-2, and 78-7.)
Supersedes NCGAI 1

Affected by: Continued in force by [GASBS 1, ¶8](#) except to the extent superseded or amended by other NCGA pronouncements

[Summary Statement of Principles No. 1](#) amended by GASBS 34, ¶6

[Summary Statement of Principles No. 2](#) amended by GASBS 34, ¶6 and ¶75

[Summary Statement of Principles No. 3](#) amended by GASBS 6, ¶13 and ¶15; GASBS 31, ¶18; and GASBS 34, ¶63; superseded by GASBS 54, ¶29–¶35

[Summary Statement of Principles No. 5](#) amended by GASBS 6, ¶13 and ¶17; GASBS 34, ¶6, ¶30, ¶69, ¶80, ¶82, ¶92, and ¶108; GASBS 63, ¶8; and GASBS 84, ¶5

[Summary Statement of Principles No. 6](#) superseded by GASBS 34, ¶18

[Summary Statement of Principles No. 7](#) superseded by GASBS 34, ¶21, ¶22, ¶92, and ¶107

[Summary Statement of Principles No. 8](#) amended by GASBS 6, ¶15; GASBS 25, ¶20, ¶25, and ¶28; GASBS 31, ¶17 and ¶18; and GASBS 34, ¶6, ¶16, ¶79, ¶92, and ¶107

[Summary Statement of Principles No. 9](#) amended by GASBS 34, ¶130

[Summary Statement of Principles No. 10](#) amended by GASBS 20, ¶6; GASBS 34, ¶6, ¶53, ¶88, ¶89, ¶100, ¶101, and ¶112; and GASBS 37, ¶10

[Summary Statement of Principles No. 11](#) amended by GASBS 34, ¶15

[Summary Statement of Principles No. 12](#) amended by GASBS 9, ¶6; GASBS 10, ¶50; GASBS 14, ¶11, ¶12, ¶19, ¶43, ¶65, and ¶66; GASBS 6, ¶25; GASBS 34, ¶6, ¶13–¶15, ¶63, ¶75, ¶80, ¶82, ¶106, and ¶125; and GASBS 61, ¶4

[Paragraph 2](#) amended by GASBS 34, ¶6

[Paragraph 3](#) amended by GASBS 34, ¶15, ¶80, and ¶82


[Paragraph 4](#) amended by GASBS 34, ¶6


[Paragraph 11](#) amended by GASBS 38, ¶9


[Paragraph 16](#) amended by GASBS 34, ¶6 and ¶75


[Paragraph 17](#) amended by GASBS 34, ¶80 and ¶82


[Paragraph 18](#) amended by GASBS 6, ¶13; GASBS 9, ¶6; GASBS 20, ¶6 and ¶7; GASBS 25, ¶11; GASBS 31, ¶18; and GASBS 34, ¶63, ¶64, ¶66, ¶69, ¶78, ¶79, ¶91–¶94, ¶106 and ¶107

Paragraph 152  superseded by GASBS 34, ¶101 and ¶112


Paragraph 153  interpreted by NCGAI 10, ¶12–¶14; amended by GASBS 14, ¶56; superseded by GASBS 34, ¶130


Paragraph 154  interpreted by NCGAI 10, ¶12–¶14; amended by GASBS 14, ¶11; superseded by GASBS 34, ¶130 and ¶131


Paragraph 155  interpreted by NCGAI 10, ¶12–¶14; amended by GASBS 14, ¶56 and GASBS 34, ¶130

Paragraph 156  amended by GASBS 9, ¶6; GASBS 14, ¶11, ¶19, ¶45, and ¶46; and GASBS 34, ¶96


Footnote 26  superseded by GASBS 9, ¶30–¶37


Paragraph 157  amended by GASBS 14, ¶51 and ¶61–¶63; GASBS 34, ¶6, ¶80, ¶82, ¶131, and ¶133; and GASBS 68, ¶47, ¶82, and ¶115


Paragraph 158  amended by NCGAI 6, ¶4 and ¶5 and all subsequent amendments to NCGAI 6; GASBS 27, ¶20–¶22; GASBI 2, ¶3; GASBS 34, ¶6, ¶113–¶123; and GASBS 38, ¶6, ¶7, ¶9, ¶10, ¶14, and ¶15

Paragraph 159  amended by GASBS 14, ¶61 and GASBS 34, ¶6, ¶80, ¶82, ¶126, and fn50


Paragraph 160  superseded by GASBS 44, ¶3


Paragraph 161  amended by GASBS 6, ¶25 and GASBS 34, ¶6; superseded by GASBS 44, ¶3

Paragraphs 162 and 163  amended by GASBS 14, ¶11, ¶51, and ¶63; superseded by GASBS 34, ¶6


Paragraph 164  amended by NCGAI 2, ¶3–¶6 and GASBS 14, ¶11, ¶51, and ¶63; superseded by GASBS 34, ¶6 and ¶122

Paragraph 165  superseded by NCGAI 2, ¶8

Paragraph 166  amended by GASBS 14, ¶11; superseded by GASBS 34, ¶6


Paragraph 167  amended by GASBS 9, ¶6; GASBS 10, ¶50; and GASBS 14, ¶19, ¶50, and ¶56; superseded by GASBS 34, ¶6

Paragraph 168  superseded by GASBS 34, ¶5

Paragraph 169  effectively amended by GASBS 1, Appendix B; superseded by GASBS 34, ¶5

Paragraph 170  amended by GASBS 9, ¶6; superseded by GASBS 34, ¶6

Paragraph 171  superseded by GASBS 34, ¶5

Paragraphs 173–175  amended by GASBS 34, ¶6

Other Interpretive Literature: GASBTB 2003-1  (Provides guidance on ¶158 )

Primary Codification Section References: Throughout

PREFACE

This Statement by the National Council on Governmental Accounting (NCGA) is a restatement of the principles of *Governmental Accounting, Auditing, and Financial Reporting* (GAAFR or the "blue book"). That 1968 pronouncement of the predecessor National Committee on Governmental Accounting, published by the Municipal Finance Officers Association (MFOA), has gained widespread acceptance and acknowledgment as the primary authoritative statement on the application of generally accepted accounting principles to state and local governments.

The GAAFR Restatement Project constitutes a modest revision to update, clarify, amplify, and reorder GAAFR in order to provide immediate guidance for governmental accounting and financial reporting. An important objective is to incorporate pertinent aspects of *Audits of State and Local Governmental Units* (ASLGU), the 1974 industry audit guide of the American Institute of Certified Public Accountants (AICPA), as amended. NCGA Statement 1 supersedes NCGA Interpretation 1, "GAAFR and the AICPA Audit Guide." Issuance of the completed *Governmental Accounting and Financial Reporting*, the restated GAAFR, with illustrative chapters for funds and other important areas of coverage is planned for late 1979.

The NCGA due process procedures were followed in developing this Statement. The NCGA issued the "GAAFR Restatement: Introduction and Principles" Working Draft in March, 1977. Council deliberations, including consideration of comments received on the working draft, led to issuance of the February, 1978 "GAAFR Restatement Principles" Exposure Draft. Comments on that exposure draft led to further council deliberations. Thus, this Statement is the result of extensive NCGA deliberations and public comment.

The GAAFR Restatement Project will be followed by the NCGA Subsequent Research Phase. This effort will involve extensive research and analysis of issues and problems that indicate a need for change from current principles and practices, and may result in significant changes in recommended governmental accounting and reporting requirements.

This Statement is effective for fiscal years ending after June 30, 1980, although earlier application is encouraged. Its provisions need not be applied to immaterial items.

INTRODUCTION

Governmental accounting is an integral branch of the accounting discipline. It is founded upon the basic concepts and conventions underlying the accounting discipline as a whole and shares many characteristics with commercial accounting.

The government environment differs markedly from that of business enterprises, however, and the information needs to be met by governmental accounting systems and reports differ accordingly.

Thus, a set of basic principles¹ applicable to governmental accounting and reporting has been developed for and utilized by governmental units. As developed by this Council and its predecessor Committees since 1934, these principles are specific fundamental tenets which, on the basis of reason, demonstrated performance, and general acceptance by public administrators, accountants, auditors, and others concerned with public financial operations, are generally recognized as essential to effective management control and financial reporting.

These basic principles are stated and explained in this Statement. These principles and illustrations provide guidance primarily for accounting and reporting for governmental operations that are different from those of business enterprises. Accounting and reporting for government operations that are similar to business enterprises closely parallel commercial accounting and reporting, and pertinent business accounting practices and professional pronouncements are applicable.

SUMMARY STATEMENT OF THE PRINCIPLES

Accounting and Reporting Capabilities

1. A governmental accounting system must make it possible both: (a) to present fairly and with full disclosure the financial position and results of financial operations of the funds and account groups of the governmental unit in conformity with generally accepted accounting principles; and

(b) to determine and demonstrate compliance with finance-related legal and contractual provisions.

Fund Accounting Systems

- ◆ 2. Governmental accounting systems should be organized and operated on a fund basis. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances, and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations.

◆ Types of Funds

3. ◆ The following types of funds should be used by state and local governments:

Governmental Funds

- (1) *The General Fund*—to account for all financial resources except those required to be accounted for in another fund.
- (2) *Special Revenue Funds*—to account for the proceeds of specific revenue sources (other than ◆ special assessments, expendable trusts, or for major capital projects) that are legally restricted to expenditure for specified purposes.
- (3) *Capital Projects Funds*—to account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by proprietary funds, ◆ Special Assessment Funds, and Trust Funds.)
- (4) *Debt Service Funds*—to account for the accumulation of resources for, and the payment of, general long-term debt principal and interest.
- ◆ (5) *Special Assessment Funds*—to account for the financing of public improvements or services deemed to benefit the properties against which special assessments are levied.

Proprietary Funds

- (6) *Enterprise Funds*—to account for operations (a) that are financed and operated in a manner similar to private business enterprises—where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.
- (7) *Internal Service Funds*—to account for the financing of goods or services provided by one department or agency to other departments or agencies of the governmental unit, or to other governmental units, on a cost-reimbursement basis.

Fiduciary Funds

■

- ◆ (8) *Trust and Agency Funds*—to account for assets held by a governmental unit in a trustee capacity or as an agent for individuals, private organizations, other governmental units, and/or other funds. These include (a) Expendable Trust Funds, (b) Nonexpendable Trust Funds, (c) Pension Trust Funds, and (d) Agency Funds.

Number of Funds

4. Governmental units should establish and maintain those funds required by law and sound financial administration. Only the minimum number of funds consistent with legal and operating requirements should be established, however, since unnecessary funds result in inflexibility, undue complexity, and inefficient financial administration.

Accounting for Fixed Assets and Long-Term Liabilities

5. A clear distinction should be made between ◆ (a) fund fixed assets and general fixed assets and (b) fund long-term liabilities and general long-term debt.
 - a. Fixed assets related to specific proprietary funds or ◆ Trust Funds should be accounted for through those funds. All other fixed assets of a governmental unit should be accounted for through the ◆ General Fixed Assets Account Group.
 - ◆ b. Long-term liabilities of proprietary funds, ◆ Special Assessment Funds, and ◆ Trust Funds should be accounted for through those funds. All other unmatured general long-term liabilities of the governmental unit should be ◆ accounted for through the General Long-Term Debt Account Group.

◆ Valuation of Fixed Assets

6. Fixed assets should be accounted for at cost or, if the cost is not practicably determinable, at estimated cost. Donated fixed assets should be recorded at their estimated fair value at the time received.

◆ Depreciation of Fixed Assets

7.
 - a. Depreciation of general fixed assets should not be recorded in the accounts of governmental funds. Depreciation of general fixed assets may be recorded in cost accounting systems or calculated for cost finding analyses; and accumulated depreciation may be recorded in the General Fixed Assets Account Group.
 - b. Depreciation of fixed assets accounted for in a proprietary fund should be recorded in the accounts of that fund. Depreciation is also recognized in those Trust Funds where expenses, net income, and/or capital maintenance are measured.

◆ Accrual Basis in Governmental Accounting

- ◆ 8. The modified accrual or accrual basis of accounting, as appropriate, should be utilized in measuring financial position and operating results.
 - a. ◆ *Governmental fund* revenues and expenditures should be recognized on the ◆ modified accrual basis. Revenues should be recognized in the accounting period in

which they become available and measurable. Expenditures should be recognized in the accounting period in which the fund liability is incurred, if measurable, except for unmatured interest on general long-term debt and on special assessment indebtedness secured by interest-bearing special assessment levies, which should be recognized when due.

- ◆ b. Proprietary fund revenues and expenses should be recognized on the accrual basis. Revenues should be recognized in the accounting period in which they are earned and become measurable; expenses should be recognized in the period incurred, if measurable.

- ◆ c. Fiduciary fund revenues and expenses or expenditures (as appropriate) should be recognized on the basis consistent with the fund's accounting measurement objective. Nonexpendable Trust and Pension Trust Funds should be accounted for on the accrual basis; Expendable Trust Funds should be accounted for on the modified accrual basis. Agency Fund assets and liabilities should be accounted for on the modified accrual basis.

- ◆ d. *Transfers* should be recognized in the accounting period in which the interfund receivable and payable arise.

Budgeting, Budgetary Control, and Budgetary Reporting

- 9. a. An annual budget(s) should be adopted by every governmental unit.
- b. The accounting system should provide the basis for appropriate budgetary control.
- ◆ c. Budgetary comparisons should be included in the appropriate financial statements and schedules for governmental funds for which an annual budget has been adopted.

Transfer, Revenue, Expenditure, and Expense Account Classification

- 10. ◆ a. Interfund transfers and proceeds of general long-term debt issues should be classified separately from fund revenues and expenditures or expenses.
- b. Governmental fund revenues should be classified by fund and source. Expenditures should be classified by fund, function (or program), organization unit, activity, character, and principal classes of objects.
- ◆ c. Proprietary fund revenues and expenses should be classified in essentially the same manner as those of similar business organizations, functions, or activities.

Common Terminology and Classification

- ◆ 11. A common terminology and classification should be used consistently throughout the budget, the accounts, and the financial reports of each fund.

Interim and Annual Financial Reports

- 12. a. Appropriate interim financial statements and reports of financial position, operating results, and other pertinent information should be prepared to facilitate management control of

management viewpoint, a governmental unit is a combination of several distinctly different fiscal and accounting entities, each having a separate set of accounts and functioning independently ♦ of other funds and account groups.

18. *Fund and Account Group Categories.* ♦ Three categories of funds are employed in governmental accounting.

- (1) *Governmental Funds*—often ♦ called "source and disposition," "expendable," or "government-type" funds—are those through which most governmental functions typically are financed. The acquisition, use, and balances of the government's expendable financial resources and the related current liabilities—except those accounted for in proprietary funds—are accounted for through governmental funds (General, Special Revenue, Capital Projects, Debt Service, and ♦ Special Assessment Funds).

Governmental funds are, in essence, accounting segregations of financial resources.

Expendable assets are assigned to the various governmental funds according to the purposes for which they may or must be used; current liabilities are assigned to the fund from which they are to be paid; and the difference between governmental fund assets and liabilities, the fund equity, is referred to as "Fund Balance."

The governmental fund measurement focus is upon determination of *financial position and changes in financial position* (sources, uses, and balances of financial resources), ♦ rather than upon net income determination. The statement of revenues, expenditures, and changes in fund balance is the primary governmental fund operating statement. It may be supported or supplemented by more detailed schedules ♦ of revenues, expenditures, transfers, and other changes in fund balance.

- (2) *Proprietary Funds*—♦ sometimes referred to as "income determination," "nonexpendable," or "commercial-type" funds—are used to account for a government's ongoing organizations and activities which are similar to those often found in the private sector (Enterprise and Internal Service Funds). ⁴ All assets, liabilities, equities, revenues, expenses, and transfers relating to the government's business and quasi-business activities—where *net income and capital maintenance are measured*—are accounted for through proprietary funds. The ♦ generally accepted accounting principles here are those applicable to similar businesses in the private sector; and the measurement focus is upon determination of net income, financial position, and ♦ changes in financial position.
- ♦ (3) *Fiduciary Funds*—♦ the Trust and Agency Funds—are used to account for assets held by a governmental unit in a trustee capacity or as an agent for individuals, private organizations, other governmental units, and/or other funds. Each Trust Fund is classified for accounting measurement purposes as either a governmental fund or a proprietary fund. Expendable Trust Funds are accounted for in essentially the same manner as governmental funds. Nonexpendable Trust Funds and ♦ Pension Trust Funds are accounted for in essentially the same manner as proprietary funds. Agency Funds are purely custodial (assets equal liabilities) and thus do not involve measurement of results of operations.

♦ 19. Accountability for and control of the government's general fixed assets and general long-term debt are accomplished through a fourth category of accounting entities, the "account groups."

- (4) *Account Groups* are used to establish accounting control and accountability for the government's general fixed assets and the unmatured principal of its ♦ general long-term debt (General Fixed Assets and General Long-Term Debt Account Groups).

The government's general fixed assets—all fixed assets except those accounted for in proprietary funds or Trust Funds—are not financial resources available for expenditure. The unmatured principal of its general long-term debt—long-term liabilities not accounted for in proprietary funds, ♦ Special Assessment Funds, or Trust Funds—does not require an appropriation or expenditure (use of financial resources) during the current accounting period.

Hence, neither is accounted for in the governmental funds, but in self-balancing account groups. These account groups are not funds—they do not reflect available financial resources and related liabilities—but are accounting records of the general fixed assets and general long-term debt, respectively, and certain associated information.

◆ 20. Eight major types of fund entities and two account group entities are employed in governmental accounting. These are considered further in [Principles 3–5](#).

21. *Separate Fund Records Required.* Each fund must be accounted for in a separate self-balancing set of accounts for its assets, liabilities, equity, revenues, expenditures or expenses (as appropriate), and transfers. This requirement of a complete set of accounts for each fund refers to identification of accounts in the accounting records, and does not necessarily extend to physical segregation of assets or liabilities. For example, it is not necessary to have a separate bank account for each fund unless required by law, bond indenture, or other reason. Likewise, governmental units utilizing system computerization and account coding techniques may treat these separate accounting entities as independent subcomponents of a unified government accounting system.

◆ 22. *Interfund Receivables and Payables.* Each fund of a governmental unit may have financial transactions and debtor-creditor relationships with other funds of the governmental unit. Interfund receivables and payables may result from services rendered by a department financed from one fund to a department financed from another fund, or from interfund loans. Interfund loans normally must be authorized by statute or ordinance. Since each fund is a fiscal and accounting entity, the amounts due to one fund from other funds, as well as the amounts owed to other funds, should be reflected in the fund accounts and in fund financial statements. ⁵

23. *Bases for Fund Establishment.* Various types of legal provisions require establishment of funds. At the state level, funds may be created pursuant to constitutional provisions or statutes enacted by the legislative body. A local government's funds may be established by state constitutional provisions or statutes, or by local charters, ordinances, and governing body orders. Funds may also be created by the governing body to achieve sound and expeditious financial administration and reporting and/or to comply with grant or contract accounting and financial reporting requirements.

24. *Classifications of Funds.* Funds may thus be distinguished according to whether they are established constitutionally, statutorily, or by other governing body action. The basis for establishing funds is particularly important when considering the discretion the chief executive officer or the governing body can exercise.

25. Another classification of funds, by fund type, takes into account both the sources of fund financial resources and the nature of activities financed. This classification is valuable in managing and controlling current financial operations and for determining compliance with applicable legal provisions. ◆ The Council recommends ◆ eight major types of funds.

◆ 26. *Types of Funds*

3. ◆ The following types of funds should be used by state and local governments:

Governmental Funds

(1) *The General Fund*—to account for all financial resources except those required to be accounted for in another fund.

(2) *Special Revenue Funds*—to account for the proceeds of specific revenue sources (other than ◆ special assessments, ◆

expendable trusts, or for major capital projects) that are legally restricted to expenditure for specified purposes.

◆ (3) *Capital Projects Funds*—to account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by proprietary funds, ◆ Special Assessment Funds, and Trust Funds.)

(4) *Debt Service Funds*—to account for the accumulation of resources for, and the payment of, general long-term debt principal and interest.

◆ (5) *Special Assessment Funds*—to account for the financing of public improvements or services deemed to benefit the properties against which special assessments are levied.

◆ Proprietary Funds

◆ (6) *Enterprise Funds*—to account for operations (a) that are financed and operated in a manner similar to private business enterprises—where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

◆ (7) *Internal Service Funds*—to account for the financing of goods or services provided by one department or agency to other departments or agencies of the governmental unit, or to other governmental units, on a cost-reimbursement basis.

Fiduciary Funds

◆ (8) *Trust and Agency Funds*—to account for assets held by a governmental unit in a trustee capacity or as an agent for individuals, private organizations, other governmental units, and/or other funds. These include (a) Expendable Trust Funds, (b) Nonexpendable Trust Funds, (c) Pension Trust Funds, and (d) Agency Funds.

27. The transactions of most of these eight fund types are planned and evaluated annually, and may be controlled by annual appropriations. To determine budgetary compliance and/or the results of financial operations, these funds must be accounted for on a fiscal year basis. Thus, the accounting